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In the Supreme Court of the United States

OCTOBER TERM, 1984

ESTATE OF DAN B. CULL, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether the decedent's gambling activities constituted a "trade or business carried on by [him]" (26 U.S.C. (1976 ed.) 62(1)) for purposes of the minimum tax on tax preferences formerly imposed by 26 U.S.C. (1976 ed.) 56 and 57.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1-8) is reported at 746 F.2d 1148. The memorandum of the Tax Court (Pet. App. 10-16) is reported at 45 T.C.M. (CCH) 691.

JURISDICTION

The judgment of the court of appeals was entered on October 23, 1984 (Pet. App. 9). The petition for a writ of certiorari was filed on January 21, 1985. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. During 1977, Dan B. Cull, now deceased,[1] was employed full time as a pari-mutuel clerk at various race tracks in northern Ohio (Pet. App. 12). He earned wages

[1]Petitioners are the decedent's surviving spouse, with whom he filed a joint federal income tax return for 1977, and the executor of his estate.

aggregating about $21,000 from those jobs (*ibid.*). He was also a habitual gambler. He devoted substantial time and energy to his race track gambling and placed wagers almost daily (*ibid.*). He bet solely for his own account and did not place bets on behalf of others or quote odds on any race (*id.* at 12-13). He incurred gambling losses in excess of his gambling winnings in 1977 (*id.* at 13).

Section 56(a) of the Internal Revenue Code, as it existed in 1977, imposed a minimum tax on persons whose "items of tax preference" exceeded certain amounts (26 U.S.C. (1976 ed.) 56(a)). Section 57(a)(1) defined "items of tax preference" to include "adjusted itemized deductions" (26 U.S.C. (Supp. I 1977) 57(a)(1)). Gambling losses (to the extent of gambling gains) are generally itemized deductions. 26 U.S.C. 63(f), 165(d). Under Section 57(b)(1)(A), however, "adjusted itemized deductions" for minimum tax purposes were defined to exclude "deductions allowable in arriving at adjusted gross income" (26 U.S.C. (Supp. I 1977) 57(b)(1)(A)). Section 62(1) in turn provided that the latter sort of deductions — often called "above the line" deductions — include deductions "attributable to a trade or business carried on by the taxpayer" (26 U.S.C. (1976 ed.) 62(1)).

The Commissioner determined that the decedent was not engaged in the "trade or business" of gambling, and hence that his gambling losses were not deductions of the type described in Section 62(1). In so concluding, the Commissioner cited *Gentile* v. *Commissioner*, 65 T.C. 1 (1975), which held that a taxpayer who gambles solely for his own account is not in a "trade or business" because he does not hold himself out to others " 'as engaged in the selling of goods or services' " (65 T.C. at 5, quoting *Deputy* v. *du Pont*, 308 U.S. 488, 499 (1940) (Frankfurter, J., concurring)). Based on this conclusion, the Commissioner determined that some of the decedent's gambling losses were

"adjusted itemized deductions," that those deductions were "items of tax preference," and the decedent was therefore liable for minimum tax.

Petitioners sought redetermination of the resulting deficiency in the Tax Court. While their petition was pending, the Tax Court overruled *Gentile* in *Ditunno* v. *Commissioner*, 80 T.C. 362 (1983), a case, like *Gentile*, involving the trade-or-business status of a full-time gambler. In *Ditunno*, the majority[2] noted that, under *Higgins* v. *Commissioner*, 312 U.S. 212 (1941), "[t]he proper test of whether an individual is carrying on a trade or business requires an examination of all the facts involved in each case" (80 T.C. at 366-367 (emphasis omitted)). Under this "facts and circumstances test," the *Ditunno* court reasoned, the "failure to provide or offer goods and services [should] not [be] sufficient by itself to find that a taxpayer is not carrying on a trade or business" (80 T.C. at 370 (footnote omitted)). The *Ditunno* Court accordingly concluded that the gambler's failure to offer goods or services to others was not dispositive, and that he was engaged in a "trade or business" for minimum tax purposes by virtue of the frequency and regularity of his gambling activities (80 T.C. at 371-372).

In the instant case, the Tax Court found that the decedent was "an 'active' gambler" who "devoted substantial time and energy to his gambling activities" (Pet. App. 15-16). Following its reasoning in *Ditunno*, the court accordingly held that, besides being in the trade or business of a parimutuel clerk, the decedent was also "in the separate trade or business of gambling" (Pet. App. 16). His gambling losses thus were not "items of tax preference" subject to minimum tax (*ibid.*).

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[2]Judge Tannenwald, the author of *Gentile*, dissented, joined by three other judges (80 T.C. at 372-377). The Commissioner was precluded from appealing the adverse decision in *Ditunno* because of a procedural problem.

The Sixth Circuit unanimously reversed (Pet. App. 1-8). It noted that the courts of appeals (like the Tax Court before *Ditunno*) have typically regarded the offer of goods or services as a prerequisite to being in a "trade or business" for tax purposes (Pet. App. 6, 8 (citing cases)). And it agreed with the view expressed by the Second Circuit in *Gajewski* v. *Commissioner*, 723 F.2d 1062, 1066-1067 (1983), cert. denied, No. 83-1715 (Oct. 1, 1984) — a case involving the trade-or-business status of a full-time gambler — that the goods-or-services requirement is an appropriate "minimum standard for determining whether a taxpayer is engaged in a trade or business" (Pet. App. 8). Since the decedent in the instant case gambled only for his own account and offered no goods or services to others, the court of appeals held that his gambling activities did not amount to a "trade or business" and that his gambling losses were thus items of tax preference subject to minimum tax (*ibid.*).

ARGUMENT

The decision below is correct. Although it conflicts with an unpublished decision of the Eleventh Circuit, the law in the courts of appeals is not sufficiently developed, and the question presented is not sufficiently important, to warrant review by this Court at this time.

1. The court of appeals correctly held that the decedent was not engaged in a "trade or business" because he did not offer goods or services to others. The phrase "trade or business," while appearing frequently in the Internal Revenue Code,[3] is defined neither in the Code nor in the regulations, and the courts have thus been left to develop its meaning on a case-by-case basis. The courts have identified several requirements that a taxpayer must meet to be

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[3] *E.g.*, I.R.C. §§ 62(1) (adjustments to gross income), 162 (trade-or-business expenses), 174 (research expenses), 280A(c)(1) (home-office deductions).

engaged in a "trade or business" for tax purposes, including the requirement that his activities be regular and continuous (*e.g.*, *Stanton* v. *Commissioner*, 399 F.2d 326 (5th Cir. 1968)) and that they be undertaken to make a profit (*e.g.*, *Bessenyey* v. *Commissioner*, 379 F.2d 252 (2d Cir.), cert. denied, 389 U.S. 931 (1967)). Still another requirement —that the taxpayer hold himself out to others as offering goods or services — finds its genesis in Justice Frankfurter's concurring opinion in *Deputy* v. *du Pont*, 308 U.S. 488, 499 (1940). Since then, the goods-or-services requirement has received general acceptance in the lower courts. The Second Circuit observed in *Gajewski* that the words "trade or business" are "commonly viewed as meaning a commercial activity in which a person seeks to earn a livelihood by furnishing goods or services to others for a price" (723 F.2d at 1065-1066 (citing cases)). And the goods-or-services requirement, the court concluded, not only describes "the universal characteristic of a businessman or trader in a free enterprise society," but also offers a standard that is "administratively workable and fair to taxpayers" (*id.* at 1066-1067).

Although this Court has never had occasion explicitly to address the goods-or-services requirement, the Court implicitly approved that formula in *Snow* v. *Commissioner*, 416 U.S. 500 (1974). The question there was the proper construction of Section 174(a)(1), which allows a deduction for research expenses incurred "in connection with [a] trade or business." The Court held that the goods-or-services requirement did not apply to Section 174(a)(1), contrasting it in that respect with Section 162(a), which allows a deduction for expenses incurred "in carrying on any trade or business." The Court noted that Section 162(a) is "more narrowly written" than Section 174(a)(1) — since it

uses the words "in carrying on" rather than "in connection with" — and remarked (416 U.S. at 502-503):

> Section 174 was enacted * * * to dilute some of the conception of "ordinary and necessary" business expenses under § 162(a) * * * adumbrated by Mr. Justice Frankfurter in a concurring opinion in *Deputy* v. *DuPont*, * * * where he said that the section in question * * * "involves holding one's self out to others as engaged in the selling of goods or services."

This case concerns Section 62(1), which, like Section 162(a), requires "carrying on" a trade or business. The goods-or-services requirement was thus properly applied here as a threshold test for determining whether the decedent was so engaged.[4]

2. Contrary to petitioners' contention (Pet. 7-10), the decision below does not conflict with this Court's decision in *Higgins* v. *Commissioner*, 312 U.S. 212 (1941), nor does it reject what petitioners describe (Pet. 8) as the *Higgins* "facts and circumstances test." The question there was whether expenses incurred by an investor in managing a large securities portfolio were deductible as trade-or-business expenses under the predecessor of Section 162(a). This Court held that they were not, reasoning that personal

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[4]There is no merit to petitioners' suggestion (Pet. 14-15) that the Commissioner has taken inconsistent positions about the goods-or-services requirement. In *Steffens* v. *Commissioner*, 707 F.2d 478 (11th Cir. 1983), and *Hornaday* v. *Commissioner*, 81 T.C. 830 (1983), the IRS successfully argued that a consultant was engaged in a "trade or business," and hence was liable for self-employment tax, even though he offered consulting services to only one corporation (707 F.2d at 481-482; 81 T.C. at 833). The Commissioner in those cases did not argue that the goods-or-services requirement could be dispensed with, but that it could be satisfied by the taxpayer's holding himself out as offering services to just one "other." Accord, *e.g.*, *Grosswald* v. *Schweiker*, 653 F.2d 58 (2d Cir. 1981).

portfolio-management is not a "trade or business" regardless of the extent of a taxpayer's wealth or the amount of time expended (312 U.S. at 218). The Court did note in *Higgins* (*id.* at 217) that "[t]o determine whether the activities of a taxpayer are 'carrying on a business' requires an examination of the facts in each case." But the court of appeals here did examine the facts of this case, holding that the decedent was not in a "trade or business" because he bet solely for his own account and did not offer services to others.

As we noted recently in *Moller* v. *United States*, 721 F.2d 810 (Fed. Cir. 1983), cert. denied, No. 83-1485 (June 18, 1984), the so-called "facts and circumstances test" that petitioners and other taxpayers have sought to derive from *Higgins* is not really a test at all, for it embodies no substantive legal standard (83-1485 Br. in Opp. at 12).[5] "It is not enough," the court below noted correctly, "to say that whether a person is engaged in a trade or business is a question of facts or circumstances. The crucial question is *what* facts and circumstances are necessary to [that] determination" (Pet. App. 6-7 (emphasis in original)). Nothing in *Higgins* forecloses the goods-or-services requirement, or any of the other requirements developed by the lower courts, as relevant legal criteria to guide the trier of fact in answering that question.[6]

3. There is likewise no merit to petitioners' suggestion (Pet. 10-14) that the lower courts are in need of guidance on what constitutes a "trade or business" for tax purposes

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[5]A copy of our brief in *Moller* is being sent to petitioners' counsel.

[6]For similar reasons, petitioners err in contending (Pet. 8-9) that the decision below conflicts with *United States* v. *Pyne*, 313 U.S. 127 (1941), and *City Bank Farmers Trust Co.* v. *Commissioner*, 313 U.S. 121 (1941). Those cases, like *Higgins*, involved investment activities, and the Court disposed of them on the basis of *Higgins* (313 U.S. at 126; 313 U.S. at 131).

generally. In determining whether a particular taxpayer is engaged in a "trade or business," the courts have naturally given different weight to different factors depending on the particular situation involved. In the case of securities investors, for example, the courts, drawing on *Higgins*, have focused especially on whether the taxpayer is a "trader" as opposed to a mere "investor." See, *e.g., Moller* v. *United States*, 721 F.2d 810 (Fed. Cir. 1983), cert. denied, No. 83-1485 (June 18, 1984). But as the court below (Pet. App. 7) and other courts (*e.g., Gajewski*, 723 F.2d at 1067 & n.8) have observed, and as we explained in our brief in *Moller* (83-1485 Br. in Opp. at 9-12), these approaches are not inconsistent with one another. They reflect reasoned responses to varied factual situations.

4. The decision below is in accord with *Gajewski* v. *Commissioner*, 723 F.2d 1062 (2d Cir. 1983), cert. denied, No. 83-1715 (Oct. 1, 1984), the only other published appellate decision addressing the question presented here. As petitioners note (Pet. 3-4), the judgment below arguably conflicts with that of the Eleventh Circuit in *Nipper* v. *Commissioner*, 47 T.C.M. (CCH) 136 (1983), aff'd mem., 746 F.2d 813 (1984) (Table), an unpublished order issued after the denial of certiorari in *Gajewski* and before the Sixth Circuit's decision here.[7] In *Nipper*, the Tax Court held that a full-time gambler was engaged in carrying on a trade or business for purposes of the minimum tax on tax preferences, and the Eleventh Circuit affirmed on the basis of the Tax Court's memorandum decision. *Nipper* v. *Commissioner*, No. 84-3067 (Oct. 11, 1984).

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[7]The petitioner in *Gajewski* sought rehearing of the denial of certiorari, alleging a conflict with *Nipper*, but rehearing was denied (No. 83-1715 (Nov. 26, 1984)). The facts involved in the instant case differ somewhat from those involved in *Nipper* and *Gajewski*, since the taxpayer in those cases was a full-time gambler with no other source of income, whereas the decedent here was employed full-time as a parimutuel clerk, and gambled only in his spare moments (Pet. App. 2-3).

In our view, there is no need for this Court to consider the question presented at this time. Absent a published appellate opinion disagreeing with *Gajewski* and the decision below, the case law in this area is not sufficiently developed to warrant this Court's review. The question presented here is now pending in two other circuits,[8] and it will be time enough for the Court to consider the issue when and if a court of appeals renders a published opinion in a taxpayer-gambler's favor.

The importance of the question presented, moreover, has been diminished by subsequent congressional enactment. In 1982, Congress revised the minimum tax law and explicitly provided that gambling losses deductible under Section 165(d) are to excluded from the minimum tax base. Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, Tit. II, § 201(a), 96 Stat. 411 (currently codified in I.R.C. § 55(b)(1)(B) and (e)(1)(A)). Thus, the narrow question presented here has been resolved legislatively for years beginning after 1982. Although the question whether a gambler is engaged in a "trade or business" continues to be relevant in other tax contexts — *e.g.*, the deductibility of travel or home-office expenses — the revenue impact in those areas is limited, a factor (among others) that led us not to seek certiorari in *Nipper*.

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[8] A district court decision in favor of the Commissioner is on appeal to the Third Circuit in *Noto* v. *United States*, 598 F. Supp. 440 (D.N.J. 1984), appeal pending, No. 84-5704 (argued May 17, 1985), and a Tax Court decision in favor of a taxpayer-gambler is on appeal to the Seventh Circuit in *Groetzinger* v. *Commissioner*, 82 T.C. 793 (1984), appeal pending, No. 84-2507 (argued Apr. 11, 1985).

CONCLUSION

The petition for a writ of certiorari should be denied.

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